




General Services Administration
Public Buildings Service
Washington, DC 20405

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MEMORANDUM FOR ALL REAL PROPERTY LEASING ACTIVITIES
(PQRP DISTRIBUTION LIST)

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COMMISSIONER - P 

SUBJECT: Use of Purchase Options in Leases

1. Purpose. This acquisition memorandum establishes policies and procedures for the use of purchase options in lease actions.
2. Background. This memorandum establishes the policy framework for the regions' use in availing themselves of market opportunities as they occur in their leasing operations. This is particularly true under soft market conditions or other favorable circumstances which may make it possible for the Government to acquire tangible benefits in the leasing of real property by obtaining purchase options. Regions should, however, continue to use sound business judgment in seeking purchase options just as in any other real estate acquisition.
3. Effective Date/Expiration Date. These instructions are effective immediately upon issuance and will expire 12 months from the date thereof, unless extended.
4. Cancellation. The following policy memoranda are cancelled:
 - a. "Purchase Options in Leases and Lease-Purchase Contracts" dated August 18, 1987.
 - b. "Purchase Options" dated September 2, 1982.
5. Applicability. All real property leasing activities which may be eligible to include purchase options.
6. Instructions/Procedures. Instructions and procedures are attached. The following is a summary of attachments:
 - a. Attachment 1 - Instructions for the Use of Purchase Options in Leases.
 - b. Attachment 2 - Sample Solicitation Language.
 - c. Attachment 3 - Guidelines for Exercising the Purchase Option.

Attachments



Attachment 1INSTRUCTIONS FOR THE USE OF PURCHASE OPTIONS IN LEASESI. Introduction.

General. Purchase options may be considered for inclusion in lease contracts when they offer the Government economic and other advantages and their attainment is consistent with the Government's goals.

II. Situations for Consideration of Purchase Options.

Projects which may be appropriate for obtaining purchase options in real property leases include those situations where the Government is the sole tenant or major tenant and the agency's mission is stable with a long-term requirement, i.e., 10 years or more.

III. Types of Purchase Options.

The following examples illustrate types of purchase options which may be considered. Variations of these approaches may also be considered:

A. Option to purchase at the end or expiration of the lease term at a fixed purchase price. The actual purchase price is negotiated, based on a projection of the property's value at the end of the lease term.

B. Option to purchase at specified intervals of the lease term at a fixed purchase price. A purchase price is negotiated for each of a number of specified intervals of the lease term, e.g., 5, 10, 15, or 20 years. The Government may exercise the purchase option at each interval at the predetermined purchase price.

C. Option to purchase with purchase price based on a formula. The value of the property is determined when the lease is executed. This may be accomplished by using a specified percentage of the appraised value in relation to the time in which the option is to be exercised. There may also be other alternate methods for determining property value with this approach.

D. Option to purchase at nominal cost. Leases with options to purchase in which the purchase price is at nominal cost may be considered for situations in which the total cost of the property is amortized over the term of the lease. Such projects may

include lease-construction, major renovation, or conversion from one type of building use to another. This situation is most likely to occur in a building where the occupancy is so unusual that there would be virtually no residual value at the end of the lease term for any owner except the Government.

IV. Lease Approval Process (Prospectus and Non-Prospectus).

A. Prospectus Level Projects. Through the regional Capital Improvement and Leasing Program, regions will submit to the Office of Planning (PL), projects involving the acquisition of leases having purchase options. The regions are responsible for making the appropriate housing recommendation after consideration of the issues related to client mission, timing, effectiveness and highest and best use of the inventory. The "OMB scoring" issue should play no part in the regions' determination of the proper business judgment for housing clients. Lease terms must be responsive to the market and be able to provide the best competitive arena for filling the need. Submission guidance will be included in the annual Capital Improvement and Leasing Program Planning Call.

Central Office will handle the approval process, including budgetary implications and related issues. PL will coordinate Central Office review of possible lease purchase options through existing prospectus review procedures. Major leases may have elements of capital investment and will be investigated by the Central Office as part of the Planning and Project Review Board approval process prior to project authorization to ensure that appropriate authorities are in place. Of course, Central Office approval is not required for projects where the Congress initiates and mandates the inclusion of a purchase option.

B. Nonprospectus Leases. With the exception of purchase options for which the purchase price is at a nominal cost, those purchase options for leases which do not require congressional approval will also not require Central Office approval. Proposed lease actions which are expected to contain options at a nominal value, or at a bargain price (little or no residual value remains in the property at the end of the lease term) will require additional budget authority. These types of transactions must be submitted to the Budget Division (PFB) and approved by the Central Office prior to advertising to ensure the appropriate budget authority is available.

For both prospectus and non-prospectus level projects, funding for the purchase must be available before the option may be exercised.

V. Preparation of Solicitation for Offers.

Market conditions in the area in which the leasehold is being acquired will be indicative of whether the market is willing and able to provide purchase options to the Government. Knowledge and use of this market information by the regions will be helpful in determining if the solicitation of leases with purchase options is viable. Where it has been determined that the attainment of a purchase option in a lease agreement will be beneficial to the Government, the advertisement for the lease, as well as the text of the SFO itself, should state that the purchase option is required, and that the submission of a purchase option will be mandatory for the offer to be considered. The foregoing applies also to those actions in which the Congress has mandated the acquisition of a lease with a purchase option. The regions shall document the file to explain its rationale in requiring the submission of a purchase option in the SFO. The SFO shall also state that the Government will not pay for the option right (opportunity costs). Additionally, the SFO must state the manner or format to be used by offerors in submitting the purchase option so that all options are submitted on the same basis, e.g., fixed purchase price, formula determination, etc.

VI. Evaluation of Offers.

Offers will be evaluated on the basis of the leasehold acquisition by considering rental and other award factors stated in the SFO. The purchase option should not comprise a part of the price evaluation for the leasehold.

The proposed purchase price will be evaluated at the time the option is to be exercised. This evaluation will include an appraisal to determine that the purchase price is fair and reasonable. The purchase price may be the subject of further negotiations between the parties shortly before the option exercise period. Further negotiations may be necessary at this time if, for instance, the appraisal required in step 5 of Attachment 3 hereof shows the offered purchase price to be out of line with current market conditions. At this point in the acquisition, the project may be considered as a building purchase and reference to the Building Purchase Policy Memorandum PQRP-89-09 dated October 6, 1989, for appropriate building acquisition guidance should be made.

VII. Funding Sources.

As stated above, PBS policy prohibits payment of opportunity costs associated with obtaining purchase options in leases. However, the purchase price itself associated with exercising the purchase option for in-cycle prospectus level acquisitions will normally be funded through a specific line item in the PBS annual authorizations act. Rental costs associated with the lease contract will be funded as usual through B/A 53, Rental of Space Account.

VIII. Records Management.

Regional Real Estate Divisions and Planning Staffs will be responsible for maintaining accurate records and for developing timelines keyed to budget/funding cycles to enable timely notification for exercising purchase options. This process also helps to ensure that all preliminary actions, such as appraisals, building inspections, and Central Office approvals, including congressional notification and approval, are accomplished.

Attachment 2SAMPLE SOLICITATION LANGUAGE

The following is suggested solicitation language. The first example requests a specific type of option, i.e., fixed price at 5-year intervals. The second example asks for an option to purchase and to be exercised at varying intervals as determined by the Government. The type of option or the period for exercising it will depend on the particular lease action and prospectus language, or other applicable directives.

Sample No. 1

Option to Purchase at 5-year intervals:

(1) "Offers are requested for a firm (20 year) lease term including a no-cost purchase option(s). A no-cost purchase option is a purchase option for which the Government does not pay for the option right. The offer must provide for purchase option(s) which may be exercised (at the end of the 5th, 10th, 15th, and 20th years). Offers which do not include the purchase option(s) will not be considered."

The purchase prices must be expressed as fixed prices for each interval.

(2) If the Government will not be the sole tenant of the building, the offeror must provide the names of other tenants, square feet occupied, and lease term expiration date.

Sample No. 2

Option to purchase at variable intervals:

(1) "Offers are requested for a firm (20 year) lease term including a no-cost purchase option(s) at one or more intervals (insert interval of _____ years) during the lease term and/or at the expiration of the lease term. A no-cost purchase option is a purchase option for which the Government does not pay for the option right. Offers which do not include the purchase option(s) will not be considered."

The purchase price must be a fixed price or a base price with adjustments that can be converted to total dollars for evaluation purposes.

(2) If the Government will not be the sole tenant of the building, the offeror must provide the names of the other tenants, square feet occupied, and lease term expiration date.

Attachment 3**GUIDELINES FOR EXERCISING THE PURCHASE OPTION**

- (1) To ensure orderly funding, regions shall submit in-cycle prospectus level acquisitions via the PPRB process for funding approval. Approximately 2 years prior to the date on which the option may be exercised, the Regional Real Estate Divisions and the Regional Planning Staffs will consult and recommend to the Administrator either: (a) to exercise the option, or (b) not exercise the option (that is defer the decision to the next option interval, for multiple interval options, or to let the option expire of its own terms). If the Administrator concurs with the recommendation to exercise the purchase option, then proceed as follows:
- (2) Submit Building Purchase Proposal Package to the Office of Planning (PL) (see Building Purchase Policy, Tab D). If funding is requested through the line-item process, the Building Purchase Proposal Package is not required.
- (3) Obtain approval from PL to proceed with preparations for exercising the option.
- (4) Obtain copies of non-Government leases in the property and provide to the Regional Counsel for review.
- (5) Order a contract appraisal for the property (see Building Purchase Policy, Paragraph D for details). Ensure that instructions are given to the appraiser not to consider any value imputed to improvements ordered and paid for by the Government during the term(s) of the lease. This appraisal will serve to confirm that the negotiated purchase price in the lease contract is fair and reasonable at the time the option is exercised.
- (6) Order Title Report and Survey of the property (see Building Purchase Policy, Paragraph F).
- (7) Order a technical inspection of the building (the Building Engineering Report format may be used, or the check list included in the Building Purchase Policy, Tab C).
- (8) Assemble an approval package which should include:
 - (a) Current net present value analysis comparing the remaining stream of rental payments to the proposed lump sum purchase price payment. This analysis should also include any elements such as operation, maintenance, capital replacement and insurance that were included in the rental payments and which become Government responsibility. (Note: A separate analysis is not necessary if the Building Purchase Proposal Package in (2) above includes all the pertinent factors.)

- (b) Summary Memorandum (similar to a price negotiation memorandum). This memorandum should summarize the reasons why it is in the best interests of the Government to exercise the purchase option at this time. Among other items it should address are the present value comparison of the purchase price to the remaining rental payments, the appraisal information, the technical inspection report and any estimates of immediate and long-term costs associated with identified repairs or replacements (do not include the cost of desired enhancements).
 - (c) Building Purchase Proposal package (previously forwarded to the Office of Facility Planning).
 - (d) Contract appraisal report.
 - (e) Engineering/technical report.
 - (f) Non-Government tenant leases.
 - (g) Report of Title and Survey together with Regional Counsel opinion on title.
 - (h) Copy of lease contract and option being exercised.
 - (i) Required regional clearance.
 - (j) Approval letter for signature of the Administrator (see Building Purchase Policy, Tab G, for a sample letter).
- (9) Prepare submittal letter from Regional Administrator to the Office of Acquisition Policy for review and submission of their comments to the Administrator.
- (10) Following the Acquisition Policy review, the Administrator will sign the authorization to proceed with exercising the option.
- (11) The contracting officer will immediately notify the lessor by certified mail of the Government's exercise of the purchase option and arrange for settlement.
- (12) The contracting officer will order a final title report and arrange with the title company to provide a final update on title immediately prior to settlement. This may be furnished by telephone or other electronics means. Any changes in title information should be immediately relayed to Regional Counsel for opinion prior to settlement. The title company should thereafter provide an official, written update of the title report. A final survey as well as title insurance should also be ordered.

(13) The contracting officer will prepare the funding documents (see Tab G of the Building Purchase Policy for sample forms).

(14) Regional Legal Counsel will prepare the appropriate instrument of conveyance, and will develop a schedule of permitted exceptions, if applicable. The lessor/offeree shall be required to do such things as provide a general warranty deed, remove mortgages, mechanics liens, charges, or encumbrances, pay taxes, and shall give assurances that the conveyance is not in violation of any agreement, instrument, mortgage, indenture, contract, judgment, decree, order, statute, rule, or governmental regulation applicable to the property. Reference to the Building Purchase Policy Memorandum PQR-89-09, dated October 6, 1989, for appropriate building acquisition guidance should be made. Regional Counsel will also initiate consultation with the Department of Justice if Counsel deems it necessary.

(15) The deed should then be recorded in the land records office of the local jurisdiction in which the property is located.